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Supreme Court of the United States

OCTOBER TERM, 1948

NO.

O. PHIL NORDLING and GILL NORDLING,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Petition for Writ of Certiorari to The United States Circuit Court of Appeals for the Ninth Circuit.

To the Honorable, The Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioners, O. Phil Nordling and Gill Nordling, respectfully petition this Honorable Court to review the final decree of the Circuit Court of Appeals for the Ninth Circuit entered upon review of a decision of The Tax Court of the United States determining a proposed deficiency in federal income tax on the return of O. Phil Nordling for the year 1941 in the amount of $592.10, and determining proposed deficiencies in federal income tax on the returns of Gill

Nordling for the calendar years 1941 and 1943 in the amounts of $62.87 and $12,807.42, respectively.

In support of this petition, the petitioners respectfully show:

I.
JURISDICTION

(a) The statutory provision sustaining the jurisdiction of this Court in this cause is Section 240 of the Judicial Code, as amended by the Act of February 13, 1925, Chapter 229, Section 1, 43 Stat. 938, United States Code, Title 28, Section 347.

(b) The date of the entry of the decree of the Circuit Court of Appeals for the Ninth Circuit here sought to be reviewed was March 23, 1948. Said decree was and is the final decree of that Court. This petition for writ of certiorari, the brief of petitioners in support of said petition, and the record in said cause are being filed in this Court within three months after the entry of said final decree in compliance with the provisions of United States Code, Title 28, Section 350.

(c) This case arises under the Internal Revenue Code, Section 22(a) (United States Code, Title 26, Section 22(a)); Section 3797(a)(2) (United States Code, Title 26, Section 3797(a)(2)); Section 23(e) (United States Code, Title 26, Section 23(e)); Section 23(g) (United States Code, Title 26, Section 23(g)); Section 117(a)(1), (b) (United States Code,

Title 26, Section 117(a)(1), (b)); and Section 24(b) (United States Code, Title 26, Section 24(b)) (Sections 22(a), 3797(a)(2), 23 (e) 23(g), 117(a)(1), (b), and 24(b) of the Internal Revenue Code, as amended, are set forth at pages 4-6 of this petition), and presents questions of law involving the construction of the above-cited federal statutes. The rulings of the Court below were such that these petitioners were and are deprived of rights, privileges and immunities claimed by them under said statutes.

(d) The jurisdiction of this Court to review said decree is sustained by said Section 240 of the Judicial Code, by subdivision (b) of Section 5 of Rule 38 of this Court, and by the decisions of this Court in *Commissioner of Internal Revenue vs. Heininger,* 320 U. S. 467, 88 L. Ed. 171, 64 S. Ct. 249; *Dobson vs. Commissioner of Internal Revenue,* 320 U. S. 489, 88 L. Ed. 248, 64 S. Ct. 239; *Commissioner of Internal Revenue vs. Bedford Estate,* 325 U. S. 283, 89 L. Ed. 1611, 65 S. Ct. 1157.

II.

SUMMARY STATEMENT OF THE MATTER INVOLVED

A. Legal Questions Presented.

This case present the following legal questions:

1. Is partnership income, distributable to a wife under a partnership agreement between said wife

and her husband, taxable to the husband under Sections 22(a)[1] and 3797(a)(2)[2] of the Internal Revenue Code pursuant to the rulings in *Lusthaus vs. Commissioner of Internal Revenue*, 327 U. S. 293, 66 S. Ct. 539, and *Commissioner of Internal Revenue vs. Tower*, 327 U. S. 280, 66 S. Ct. 532, where such income is derived from property purchased by the wife from a party other than the husband and contributed to the partnership by the wife as her own separate property under state constitutional and statutory provisions.

2. Is income in the form of dividends derived from stock of a corporation by a wife taxable to the husband under Section 22(a) of the Internal Revenue Code pursuant to the rulings in *Lusthaus vs. Com-*

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1. Section 22(a) of the Internal Revenue Code provides insofar as material here:

"§22. Gross income

"(a) General definition. 'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *"

2. Section 3797(a)(2) of the Internal Revenue Code, insofar as material here, provides:

"§3797. Definitions

"(a) When used in this title, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof— * * *

"(2) Partnership and partner. The term 'partnership' includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this title, a trust or estate or a corporation; and the term 'partner' includes a member in such a syndicate, group, pool, joint venture, or organization."

missioner of Internal Revenue, supra, and *Commissioner of Internal Revenue vs. Tower, supra,* where said stock was purchased by the wife from a party other than the husband and was owned by the wife as her separate property, under state constitutional and statutory provisions, at the time of the derivation of income.

3. Is a long-term capital loss sustained by a taxpayer, and otherwise claimable by said taxpayer under Section 23(e)(g)[3] and Section 117[4] of the Internal Revenue Code legally denied under Section 24(b)[5] of the Internal Revenue Code solely because the taxpayer sold stock of a corporation, on which the loss was claimed, to his sister-in-law in the same transaction in which other shares of the same stock were sold to the taxpayer's brother.

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3. Section 23(e)(g) of the Internal Revenue Code provides insofar as material here:

"§23. Deductions from gross income. In computing net income there shall be allowed as deductions: * * *

"(e) Losses by individuals. In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

"(1) if incurred in trade or business; or

"(2) if incurred in any transaction entered into for profit, though not connected with the trade or business; * * *.

"(g) Capital losses.

"(1) Limitation. Losses from sales or exchanges of capital assets shall be allowed only to the extent provided in section 117.

"(2) Securities becoming worthless. If any securities (as defined in paragraph (3) of this subsection) become worthless during the taxable year and are capital assets, the loss resulting therefrom shall, for the purposes of this chapter, be considered as a loss from the sale or exchange, on the last day of such taxable year, of capital assets.

"(3) Definition of securities. As used in this subsection the term 'securities' means (A) shares of stock in a corporation, and (B) rights to subscribe for or to receive such shares."

4. Section 117 of the Internal Revenue Code, insofar as material here, provides:

B. Summary of Facts Involved.

O. Phil Nordling (hereinafter referred to as Phil) and Gill Nordling (hereinafter referred to as Gill) operated an auto parts and accessories business as co-partners at Eugene, Oregon, and Roseburg, Oregon, under the name of Nordling Parts Co. from February, 1939, to and including September 1, 1941

"§117. Capital gains and losses

"(a) Definitions. As used in this chapter—

"(1) Capital assets. The term 'capital assets' means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23(*l*) or an obligation of the United States or any of its possessions, or of a State or Territory, or any political subdivision thereof, or of the District of Columbia, issued on or after March 1, 1941, on a discount basis and payable without interest at a fixed maturity date not exceeding one year from the date of issue, or real property used in the trade or business of the taxpayer; * * *

"(b) Percentage taken into account. In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net capital gain, net capital loss, and net income:

"100 per centum if the capital asset has been held for not more than 6 months;

"50 per centum if the capital asset has been held for more than 6 months."

5. Section 24(b) of the Internal Revenue Code, insofar as material here, provides:

"§24. Items not deductible * * *

"(b) Losses from sales or exchanges of property.

"(1) Losses disallowed. In computing net income no deduction shall in any case be allowed in respect of losses from sales or exchanges of property, directly or indirectly—

"(A) Between members of a family, as defined in paragraph (2)(D); * * *

"(2) Stock ownership, family, and partnership rule. For the purposes of determining, in applying paragraph (1), the ownership of stock— * * *

"(D) The family of an individual shall include only his brothers and sisters (whether by the whole or half blood), spouse, ancestors, and lineal descendants; * * *."

(R. 50-51). On September 1, 1941, Phil owned 132 shares of common stock and 9 shares of preferred stock of Nordling Finance Co., an Oregon corporation, and on said date Gill owned 106 shares of common stock and 7 shares of preferred stock of said corporation (R. 60-61; Pet. Ex. No. 5). On September 16, 1941, an agreement was executed wherein Phil agreed to sell to Gill and Bernice E. Nordling (hereinafter referred to as Bernice), and Gill and Bernice agreed to purchase from Phil, the one-half interest of Phil in the partnership known as Nordling Parts Co. and the 132 shares of common stock and 9 shares of preferred stock of Nordling Finance Co. owned by Phil (R. 54-55; Pet. Ex. No. 1). Gill and Bernice are husband and wife (R. 152). The aforementioned agreement executed on September 16, 1941, transferred ownership of Phil's partnership interest and stock as of September 2, 1941 (R. 54-55; Pet. Ex. No. 1).

The agreement of September 16, 1941 was consummated as the result of negotiations between Phil and Gill by letter in the period from August 1, 1941, to August 28, 1941, both dates inclusive (R. 85-88; Resp. Exs. Nos. A, B, C, D, E). Phil made an offer to Gill to sell his partnership interest and stock to Gill for $18,500.00, or buy Gill's partnership interest and stock for $18,500.00, at the election of Gill (R. 85-88; Resp. Exs. Nos. D, E). Phil's offer was made pursuant to the terms of the partnership agreement entered into in 1939 between Phil and Gill (R. 88-89;

Resp. Ex. No. F). Upon receipt of Phil's offer in letter dated August 19, 1941, Gill made an offer to Bernice to join with him (Gill) in the purchase of Phil's partnership interest and stock (R. 52-53, 152-154). Bernice accepted Gill's offer to join with Gill in the purchase of Phil's partnership interest and stock (R. 52-53, 152-154). Phil knew prior to the execution of the agreement of September 16, 1941, that the prospective purchasers with whom he was dealing were Gill and Bernice (R. 132-134). Phil executed said agreement with the intention of conveying his partnership interest and stock to Gill and Bernice as joint purchasers (R. 132-133, 138-139). Phil in fact executed the documents consummating the sale to and with Gill and Bernice as joint purchasers (R. 53-60; Pet. Exs. Nos. 1, 2, 3, 4, 5). Phil accepted assignments executed by Bernice as security for the note given by Gill and Bernice pursuant to the agreement of sale (R. 61-63; Pet. Ex. No. 6).

The aforementioned agreement executed September 16, 1941, was fully performed by both the seller and purchasers. On September 16, 1941, Phil executed and delivered to Gill and Bernice a bill of sale whereby all right, title and interest of Phil in the partnership known as Nordling Parts Co., and in the business and assets of said partnership, were conveyed to Gill and Bernice (R. 58-59; Pet. Ex. No. 4). Phil delivered to Gill and Bernice certificates for 132 shares of common stock and 9 shares of preferred stock of Nordling Finance Co., an Oregon

corporation (R. 59-60; Pet. Ex. No. 5). Pursuant to said agreement, Gill and Bernice paid Phil a down payment of $3,000.00 and executed and delivered to Phil a promissory note dated September 2, 1941, in principal amount of $15,500.00, payable at the rate of $150.00 per month with interest at the rate of 4% per annum on the unpaid balance of principal (R. 55-58; Pet. Exs. Nos. 2, 3). The note delivered to Phil was executed by Gill and Bernice as co-makers (R. 55; Pet. Ex. No. 2). $2,950.00 of the down payment was paid with proceeds of a bank loan (R. 56-57; Pet. Ex. No. 3). The bank note was executed by Gill and Bernice as individual co-makers and as officers of Nordling Finance Co., a corporation (R. 56-57; Pet. Ex. No. 3). The balance of the bank loan in amount of $4,000.00, in excess of the down payment of $2,950.00, was applied by Gill and Bernice on amounts due Phil under the agreement of September 16, 1941, in addition to the purchase price of $18,500.00 (R. 57; Pet. Ex. No. 1). The note delivered to Phil was paid in full out of profits of Nordling Parts Co. during the period from September 16, 1941, to August 26, 1944, both dates inclusive (R. 126-128; Pet. Exs. Nos. 26, 29). The payments on said note were charged to the drawing accounts of Gill and Bernice on the books of Nordling Parts Co. (R. 127-128; Pet. Ex. No. 29). The bank note was paid in full during the period from September 12, 1941, to December 31, 1941 (R. 125-126; Pet. Ex. No. 18). Gill and Bernice borrowed the money to pay the bank

loan from Nordling Finance Co., and thereafter paid the loan from the corporation, with interest, out of profits of Nordling Parts Co. (R. 127-128, 146-148; Pet. Ex. No. 29). The amount applied in repayment of the loan from Nordling Finance Co. was charged to the drawing accounts of Gill and Bernice on the books of Nordling Parts Co. (R. 127-128; Pet. Ex. No. 29).

The note for $15,500.00 executed and delivered by Gill and Bernice to Phil was secured by assignments of 131 shares of common stock and 9 shares of preferred stock of Nordling Finance Co., a corporation (R. 62-63; Pet. Ex. No. 6). Gill executed and delivered to Phil an assignment of 65 shares of common stock and an assignment of 4½ shares of preferred stock (R. 62-63; Pet. Ex. No. 6). Bernice executed and delivered to Phil an assignment of 66 shares of common stock and an assignment of 4½ shares of preferred stock (R. 62-63; Pet. Ex. No. 6). The bank note was secured by a promissory note in amount of $22,000.00, which belonged to Nordling Finance Co., a corporation, and was in the possession of the bank as escrow agent for collection (R. 82-83, 116-118).

At all times herein material on and after September 2, 1941, Bernice exercised the incidents of ownership with respect to the property acquired by her from Phil pursuant to the agreement executed on the last mentioned date. Bernice entered into a written agreement of general partnership with Gill on

September 10, 1941, whereunder she conveyed to the partnership the interest in Nordling Parts Co., and in the business and assets of said company, which she acquired from Phil (R. 66-67; Pet. Ex. No. 9). Pursuant to the partnership agreement, Bernice contributed to the partnership one-fourth of the initial capital thereof in the amount of $6,340.22, which said capital so contributed was one-half of the 50% interest in the company acquired by Bernice and Gill under the agreement of September 16, 1941 (R. 66-67; Pet. Ex. No. 9). The capital accounts of Bernice and Gill in the partnership were equalized on January 15, 1943, by a gift of partnership capital from Gill to Bernice in amount of $4,872.49 (R. 129; Pet. Ex. No. 35). The gift was reported pursuant to the federal gift tax statutes (R. 129; Pet. Ex. No. 35). The stock certificates, representing 131 shares of common stock and 9 shares of preferred stock, delivered by Phil to Gill and Bernice were surrendered to the corporation and new certificates issued as follows: Bernice, 66 shares of common and 4½ shares of preferred; Gill, 65 shares of common and 4½ shares of preferred (R. 59-60; Pet. Ex. No. 5). The certificate for one qualifying share outstanding in the name of Spencer R. Collins, delivered by Phil to Gill and Bernice, was left outstanding in the name of Spencer R. Collins (R. 59-60; Pet. Ex. No. 5). Bernice assigned the 66 shares of common stock and 4½ shares of preferred stock to Phil to secure the note executed and delivered to Phil (R. 62-63; Pet.

Ex. No. 6). At all times herein material from and after September 2, 1941, the books of account of Nordling Parts Co. were kept on the partnership basis and reflected the capital and drawing accounts of Gill and Bernice (R. 127-129; Pet. Exs. Nos. 29, 30, 32, 33). One-half of the income of the partnership, realized on and after September 2, 1941, was credited to the capital and drawing accounts of Bernice on the books of the partnership (R. 127-128; Pet. Exs. Nos. 29, 30). Bernice made periodical withdrawals from her share of the income of the partnership and such withdrawals were charged to her accounts on the books of the partnership (R. 127-129; Pet. Exs. Nos. 29, 30, 32, 33).

From and after September 2, 1941, Gill and Bernice operated Nordling Parts Co. as a general partnership. The assumed business name certificates recording Phil as a partner in the company were withdrawn (R. 63-64; Pet. Ex. No. 7). New assumed business name certificates were filed recording Gill and Bernice as partners in the company (R. 64-66; Pet. Ex. No. 8). Bank loans obtained by the company after September 2, 1941, were obtained on the signatures of Gill and Bernice (R. 126; Pet. Exs. Nos. 19, 20, 21, 22). The signature card filed by Nordling Parts Co. with the bank authorized both Gill and Bernice to sign checks on the company's bank account (R. 126; Pet. Ex. No. 23). Contracts executed by the company with manufacturers appertaining to the company's rights as a distributor were all

executed in the name of Nordling Parts Co. by Gill Nordling, partner (R. 102-106). Reports were filed with Dun & Bradstreet in the name of Gill Nordling and Bernice E. Nordling doing business as Nordling Parts Co. (R. 73; Pet. Ex. No. 13). The change in ownership of Nordling Parts Co. from Phil and Gill to Gill and Bernice was registered with Income Tax Withholding Division, Collector of Internal Revenue, Social Security Division, Collector of Internal Revenue, and State Unemployment Compensation Commission (R. 71). Leases on the store sites in Eugene and Roseburg were assigned to Gill and Bernice (R. 74-75; Pet. Exs. Nos. 14, 15). New leases on said store sites were obtained in the names of Gill and Bernice as lessees (R. 76-78). A trust creating and governing a plan of employee benefits was executed by Gill and Bernice as owners of Nordling Parts Co. (R. 80). The customers of Nordling Parts Co. were informed of the change in ownership of the company from Phil and Gill to Gill and Bernice (R. 106-107).

After the formation of the partnership between Gill and Bernice on September 10, 1941, Bernice participated in the business as a general partner. Bernice participated in the decision that Phil's offer to sell his partnership interest and stock be accepted (R. 53). She exercised her judgment and decision with respect to matters appertaining to the management and control of partnership business (R. 53, 79-80, 152-153). She rendered personal services in

the course of the partnership business (R. 79-80, 152-153, 157-158). After the acquisition of Phil's stock in Nordling Finance Co., Bernice became an officer of said corporation and acted in that capacity (R. 56-57; Pet. Ex. No. 3). She made withdrawals from her share of the profits of the partnership and deposited the amounts so withdrawn in her personal bank account (R. 154-157; Pet. Exs. Nos. 41, 42).

Nordling Parts Co. engaged, during the years here involved, in the business of selling automotive parts and accessories at wholesale and retail (R. 94-97; 102-106). The invested capital of Nordling Parts Co. on the various dates herein material was as follows (R. 128-129; Pet. Exs. Nos. 32, 33):

Date	*Total*	*Net*
September 2, 1941	$55,784.74	$25,265.98
December 31, 1941	55,692.69	21,535.13
December 31, 1942	60,984.65	40,530.44
December 31, 1943	97,570.94	52,177.77

The inventory of merchandise maintained by the company on the various dates herein material was as follows (R. 128-129; Pet. Exs. Nos. 32, 33):

Date	*Inventory*
September 4, 1941	$34,048.02
December 31, 1941	33,361.31
December 31, 1942	39,635.85
December 31, 1943	68,840.28

On September 2, 1941, the book value of Phil's partnership interest and stock was in excess of the purchase price of $18,500.00 paid by Gill and Bernice (R. 102, 123, 136, 143, 128-129; Pet. Exs. Nos. 32, 34). The bank was aware that the partnership assets were of a value substantially in excess of the $4,000.00 loan made to Gill and Bernice to make the down payment to Phil (R. 123). An asset owned by Nordling Finance Co., a corporation, was made security for said bank loan at the insistence of the bank in compliance with usual bank practice of seizing on all available security regardless of the size of the loan (R. 118-119).

Prior to the acceptance of Phil's offer to sell his partnership interest and stock by Gill and Bernice, Gill consulted with his accountant on the matter of Gill and Bernice forming a partnership (R. 144). The suggestion that Bernice be taken into the partnership did not originate with the accountant (R. 144-145). The tax saving motive was not the primary reason for taking Bernice into the partnership (R. 144-145).

III.

REASONS RELIED ON FOR ALLOWANCE OF WRIT

Petitioners submit that this Court should review said decree of the United States Circuit Court of Appeals for the Ninth Circuit for the following reasons:

1. With respect to the issue of the taxability to Gill Nordling, the husband, of partnership income of Nordling Parts Co. distributable to Bernice Nordling, the wife, under the partnership agreement—

(a) In deciding that partnership income derived by the wife from property purchased by her from a party other than the husband, and contributed to the partnership by the wife as her own separate property under state constitutional and statutory provisions, is taxable to the husband, the United States Circuit Court of Appeals for the Ninth Circuit rendered a decision in conflict with the decision of the United States Circuit Court of Appeals for the Eighth Circuit in *Durwood vs. Commissioner of Internal Revenue,* 159 F. (2d) 400.

(b) In deciding that partnership income derived by the wife from property purchased by her from a party other than the husband, and contributed to a partnership by the wife as her own separate property under state constitutional and statutory provisions, is taxable to the husband, the United States Circuit Court of Appeals for the Ninth Circuit has decided a federal question in a way in conflict with applicable decisions of this Court in *Lusthaus vs. Commissioner of Internal Revenue,* 327 U. S. 293, 66 S. Ct. 539 and *Commissioner of Internal Revenue vs. Tower,* 327 U. S. 280, 66 S. Ct. 532.

(c) In deciding that partnership income derived by the wife from property purchased by her from a

party other than the husband, and contributed to a partnership by the wife as her own separate property under state constitutional and statutory provisions, is taxable to the husband, The Tax Court of the United States has so far departed from the accepted and usual course of judicial proceedings as established by said Court in such cases as *Alexander vs. Commissioner of Internal Revenue,* 6 T. C. 804, *Shulak vs. Commissioner of Internal Revenue,* Tax Court Memorandum Decision, Docket No. 6654, April 30, 1946, 1946 Prentice-Hall Tax Court Memorandum Decisions, para. 46,101, and *Forsythe vs. Commissioner of Internal Revenue,* 10 T. C. No. 54, and the United States Circuit Court of Appeals for the Ninth Circuit has so far sanctioned such a departure by said lower court, as to call for an exercise by this Court of its power of supervision.

2. With respect to the issue of the taxability to Gill Nordling, the husband, of income in the form of dividends derived from stock of a corporation owned by Bernice Nordling, the wife, at the time of the derivation of the income—

(a) In deciding that income in the form of dividends derived from stock of a corporation purchased by the wife from a party other than the husband, and owned by the wife at the time of the derivation of income as her separate property under state constitutional and statutory provisions, is taxable to the husband, the United States Circuit Court

of Appeals for the Ninth Circuit rendered a decision in conflict with the decision of the United States Circuit Court of Appeals for the Fifth Circuit in *Allen vs. Beazley*, 157 F. (2d) 970, and in conflict with the decision of the United States Circuit Court of Appeals for the Sixth Circuit in *Commissioner of Internal Revenue vs. Hart*, 76 F. (2d) 864.

(b) In deciding that income in the form of dividends derived from stock of a corporation purchased by the wife from a party other than the husband, and owned by the wife at the time of the derivation of income as her separate property under state constitutional and statutory provisions, is taxable to the husband, The Tax Court of the United States has so departed from the accepted and usual course of judicial proceedings as established by said Court in such cases as *Greene vs. Commissioner of Internal Revenue*, 7 T. C. 142, *Rosborough vs. Commissioner of Internal Revenue*, 8 T. C. 136, *Sandberg vs. Commissioner of Internal Revenue*, 8 T. C. 423, *Woosley vs. Commissioner of Internal Revenue*, Tax Court Memorandum Decision, Docket No. 2981, December 6, 1946, 1946 Prentice-Hall Tax Court Memorandum Decisions, para. 46,283, and *Boozer vs. Commissioner of Internal Revenue*, Tax Court Memorandum Decision, Docket No. 9297, August 28, 1947, 1947 Prentice-Hall Tax Court Memorandum Decisions, para. 47,248, and the United States Circuit Court of Appeals for the Ninth Circuit has so far

sanctioned such a departure by said lower court, as to call for an exercise by this Court of its power of supervision.

(c) In deciding that income in the form of dividends derived from stock of a corporation purchased by the wife from a party other than the husband, and owned by the wife at the time of the derivation of income as her separate property under state constitutional and statutory provisions, is taxable to the husband, the United States Circuit Court of Appeals for the Ninth Circuit has decided an important question of federal law which has not been, but should be, settled by this Court.

3. With respect to the issue of the disallowance to O. Phil Nordling of a long-term capital loss on the sale of capital stock of Nordling Finance Co., an Oregon corporation—

(a) In deciding that a long-term capital loss otherwise claimable by a taxpayer under Section 23(e)(g) and Section 117 of the Internal Revenue Code is subject to disallowance under Section 24(b) of the Internal Revenue Code, where said taxpayer sells stock of a corporation on which the loss is claimed to his sister-in-law in the same transaction in which other shares of the same stock are sold to the taxpayer's brother, The Tax Court of the United States has so far departed from the accepted and usual course of judicial proceedings as established by said Court in such cases as *Simister, Jr., vs. Commission-*

er of Internal Revenue, 4 T. C. 470, and *Saul vs. Commissioner of Internal Revenue,* Tax Court Memorandum Decision, Docket No. 7679, June 26, 1947, 1947 Prentice-Hall Tax Court Memorandum Decisions, para. 47,178, and the United States Circuit Court of Appeals for the Ninth Circuit has so far sanctioned such a departure by said lower court, as to call for an exercise by this Court of its power of supervision.

(b) In deciding that a long-term capital loss otherwise claimable by a taxpayer under Section 23(e)(g) and Section 117 of the Internal Revenue Code is subject to disallowance under Section 24(b) of the Internal Revenue Code, where said taxpayer sells stock of a corporation on which the loss is claimed to his sister-in-law in the same transaction in which other shares of the same stock are sold to the taxpayer's brother, the United States Circuit Court of Appeals for the Ninth Circuit has decided an important question of federal law which has not been, but should be, settled by this Court.

PRAYER

WHEREFORE, your petitioners respectfully pray that a writ of certiorari be issued by this Honorable Court directed to the United States Circuit Court of Appeals for the Ninth Circuit commanding that Court to certify and to send to this Court for its review and determination a full and complete tran-

script of the record and proceedings in the case entitled on its docket *"O. Phil Nordling, Petitioner, vs. Commissioner of Internal Revenue, Respondent, Gill Nordling, Petitioner, vs. Commissioner of Internal Revenue, Respondent,* No. 11696", and that this Court review and decide the federal questions presented and reverse the decree of the United States Circuit Court of Appeals for the Ninth Circuit entered in said cause, and that the petitioners may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

O. PHIL NORDLING,
GILL NORDLING,
By CARL E. DAVIDSON,
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Supreme Court of the United States

OCTOBER TERM, 1948

NO.

O. PHIL NORDLING and GILL NORDLING,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

REPORT OF OPINIONS BELOW

The opinion of The Tax Court of the United States is officially reported in final form as Tax Court Memorandum Opinion, Docket Nos. 9310, 9316, and reprints thereof are to be found in 1947 Prentice-Hall Tax Court Memorandum Decision Service, paragraph 47,046, and on pages 166 to 185, inclusive, of the printed Transcript of Record. The opinion of the United States Circuit Court of Appeals is officially reported in final form at 166 F. (2d) 703 and a reprint thereof is to be found at pages 210 to 213, inclusive, of the printed Transcript of Record.

JURISDICTIONAL STATEMENT

A concise statement of the grounds on which the jurisdiction of this Court is invoked is set out in the foregoing petition, pages 2-3.

STATEMENT OF THE CASE

The pertinent facts are stated in the foregoing petition at pages 3-15.

SPECIFICATION OF ERRORS

The United States Circuit Court of Appeals erred:

1. In deciding that there is a deficiency in federal income tax of $592.10 for the calendar year 1941 with respect to O. Phil Nordling, and in deciding that there are deficiencies in federal income taxes of $62.87 for the calendar year 1941 and of $12,807.42 for the calendar year 1943 with respect to Gill Nordling.

2. In taxing to Gill Nordling partnership income distributable to and owned by Bernice Nordling, and in taxing to Gill Nordling dividends derived from corporate stock owned by Bernice Nordling.

3. In disallowing a long-term capital loss claimed by O. Phil Nordling and incurred by said taxpayer on the sale of corporate stock to Bernice Nordling.

4. In deciding that no bona fide partnership existed between Gill Nordling and Bernice Nordling which can be recognized for federal income tax purposes.

5. In deciding that Bernice Nordling was a mere nominal party to the transaction involving the sale of a one-half interest in the assets of Nordling Parts Co. and the stock of Nordling Finance Co., and that the only real parties in interest to said transaction were O. Phil Nordling, as seller, and Gill Nordling, as buyer.

6. In deciding that Bernice Nordling contributed no capital to the partnership formed by agreement between Gill Nordling and Bernice Nordling and known as Nordling Parts Co., and in deciding that the property purchased by Bernice Nordling from O. Phil Nordling and contributed by said purchaser to the partnership did not constitute capital originating with Bernice Nordling.

7. In deciding that the partnership formed between Gill Nordling and Bernice Nordling was organized upon the advice of an accountant and tax consultant for the purpose of effecting savings in income tax.

8. In deciding that the sale of partnership assets and corporation stock by O. Phil Nordling to Bernice Nordling was an artificial transaction because Gill Nordling, the husband of Bernice Nordling, handled the negotiations for the sale.

9. In deciding that the real ownership of the partnership assets and corporation stock purchased by Bernice Nordling from O. Phil Nordling vested in Gill Nordling, and that said property did not consti-

tute the separate property of Bernice Nordling.

10. In deciding that this case is governed by the rules formulated in *Lusthaus vs. Commissioner of Internal Revenue,* 327 U. S. 293, 66 S. Ct. 539 and *Commissioner of Internal Revenue vs. Tower,* 327 U. S. 280, 66 S. Ct. 532.

ARGUMENT

The United States Circuit Court of Appeals for the Ninth Circuit affirmed the decision of The Tax Court of the United States on the grounds that "In tax matters the realities of a transaction, not artificialities, are given effect" (R. 213). The Tax Court of the United States sustained the determinations of tax deficiencies by the Respondent because "We are persuaded by a consideration of all the facts before us that Mrs. Nordling did not, by reason of the transaction described above, become the owner of either the partnership interest claimed for her, or of the corporate stock, in such a real sense as to be recognized as owner under the Federal revenue laws" (R. 181). The Tax Court was persuaded by "the fact that the purchase of such interests was negotiated almost to completion by the husband in his own name and on his own behalf, pursuant to the terms of a partnership agreement to which he was a party" (R. 180). The Circuit Court of Appeals was equally persuaded by the manner in which the negotiations were handled (R. 211-212).

An analysis of the evidence adduced at trial (R. 49-165, and original exhibits) reveals that Bernice Nordling complied with every legal requirement necessary to the acquisition of the real ownership of property in a definitive transaction. If there was anything which Bernice Nordling failed to do to acquire the real ownership of an undivided one-half interest in the partnership assets and stock transferred by O. Phil Nordling, then such deficiency is unknown to the law governing the conveyance of property as such law exists in the State of Oregon. Nevertheless, the Circuit Court of Appeals ignored the unquestionable legal results attained by the execution and delivery of the various legal documents in evidence in this case and held that, "for federal income tax purposes", Bernice Nordling did not acquire the real ownership of the assets.

In other words, substantial tax liability is here predicated, not on the normal legal results of existing facts, but on the ability of the Court to piece out some indefinable atmospheric condition of unreality. The federal income tax statutes embody the basic principle that income from property is taxable to the owner of the property. The basic principle is invariably asserted to protect the public revenue. Nevertheless, it is now decided that the mere existence of the marital relationship is sufficient grounds for taxing to a husband income from property owned by the wife. The petition, in support of which this brief is submitted, is filed in confidence

that this Court will decide the rights of the petitioners here involved on the basis of the facts as they appear from the record, and not on a vague theory that, "for federal income tax purposes", an existing fact can be held not to exist by the simple expedient of labelling it unreal.

The lower Court concluded that Bernice Nordling, the wife, was not a real party in interest to the purchase of the partnership assets and stock because Gill Nordling, the husband, negotiated the sale "in his own name and on his own behalf". In so concluding, the Court ignored the obvious truth that legal rights are not acquired, or their acquisition given effect for tax or any other legal purpose, on the basis of who did the negotiating. The controlling factor is who, in fact, purchased the property? The evidence is unequivocal and undisputed that Gill and Bernice agreed to purchase the property jointly prior to the acceptance of Phil's offer on August 28, 1941 (R. 52-53, 152-153). Thus, in accepting the offer, Gill acted in his own behalf and in behalf of Bernice as her agent. That an agent may so contract for his principal, whether the principal be disclosed or undisclosed to the other party, is well established in law. Bernice could have sued and enforced the executory contract to sell, consummated by the acceptance on August 28, 1941, against Phil. *In Re Assignment of Pendleton Hardware Co.*, 24 Or. 330, 33 Pac. 544; *Kitchen vs. Holmes*, 42 Or. 252, 70 Pac. 830; *Levy vs. Nevada-California-Oregon Ry.*, 81 Or.

673, 160 Pac. 808; *Mercer vs. Germania Ins. Co.*, 88 Or. 410, 171 Pac. 412; 2 Am. Jur. 320 (Agency, Section 410). Equally, Phil could have sued and enforced said executory contract to sell against Bernice. *McLeod vs. Despain*, 49 Or. 536, 90 Pac. 492, 92 Pac. 1088; 2 Am. Jur. 308 (Agency, Section 394).

Moreover, income tax consequences arise from the consummation of sales of property and not from executory contracts to sell. See Internal Revenue Code, Sections 22, 24, 111, 112 (United States Code, Title 26, Sections 22, 24, 111, 112). The Uniform Sales Act (Section 71-101 et seq., Oregon Compiled Laws Annotated) defines a contract to sell and a sale as follows:

> "(1) A contract to sell goods is a contract whereby the seller agrees to transfer the property in goods to the buyer for a consideration called the price.
>
> "(2) A sale of goods is an agreement whereby the seller transfers the property in goods to the buyer for a consideration called the price.
>
> "(3) A contract to sell or a sale may be absolute or conditional.
>
> "(4) There may be a contract to sell or a sale between one part owner and another."

Likewise, the Uniform Stock Transfer Act (Section 78-101 et seq., Oregon Compiled Laws Annotated) specifies the manner in which title to shares of stock may be transferred as follows:

"Title to a certificate and to the shares represented thereby can be transferred only:

"(a) By delivery of the certificate indorsed either in blank or to a specified person by the person appearing by the certificate to be the owner of the shares represented thereby, or

"(b) By delivery of the certificate and a separate document containing a written assignment of the certificate or a power of attorney to sell, assign, or transfer the same or the shares represented thereby, signed by the person appearing by the certificate to be the owner of the shares represented thereby. Such assignment or power of attorney may be either in blank or to a specified person.

"The provisions of this section shall be applicable, although the charter or articles of incorporation or code of regulations or bylaws of the corporation issuing the certificate and the certificate itself provide that the shares represented thereby shall be transferable only on the books of the corporation or shall be registered by a registrar or transferred by a transfer agent."

Moreover, there is no question but that Bernice was endowed with full legal capacity to contract with respect to said purchase of property. Thus,

Section 71-102, Oregon Compiled Laws Annotated (Uniform Sales Act) provides in part as follows: "Capacity to buy and sell is regulated by the general law concerning capacity to contract, and to transfer and acquire property." Article XV, Section 5, of the Constitution of the State of Oregon provides: "The property and pecuniary rights of every married woman, at the time of marriage, or afterward acquired by gift, devise, or inheritance, shall not be subject to the debts or contracts of the husband; and laws shall be passed providing for the registration of the wife's separate property." The constitutional mandate was carried out by the enactment of statutes as follows:

Section 63-202, Oregon Compiled Laws Annotated, as amended by Oregon Laws 1941, Ch. 228:

> "All laws which impose or recognize civil disabilities upon a wife which are not imposed or recognized as existing as to the husband hereby are repealed, and all civil rights belonging to the husband not heretofore conferred upon the wife, or which she does not have at common law, hereby are conferred upon her, including, among other things, the right of action for loss of consortium of her husband; and for any unjust usurpation of her property or natural or civil rights she shall have the same right to appeal in her own name alone to the courts of law or equity for redress that the husband has."

Section 63-203, Oregon Compiled Laws Annotated:

"The property, either real or personal, acquired by any married woman during coverture, by her own labor, shall not be liable for the debts, contracts, or liabilities of her husband; but shall in all respects be subject to the same exemptions and liabilities as property owned at the time of her marriage or afterwards acquired by gift, devise or inheritance."

Section 63-204, Oregon Compiled Laws Annotated:

"The property and pecuniary rights of every married woman at the time of her marriage or afterwards acquired shall not be subject to the debts or contracts of her husband, and she may manage, sell, convey, or devise the same by will to the same extent and in the same manner that her husband can, property belonging to him."

Section 63-205, Oregon Compiled Laws Annotated:

"When property is owned by either husband or wife, the other has no interest therein which can be the subject of contract between them, or such interest as will make the same liable for the contracts or liabilities of either the husband or wife who is not the owner of the property, except as provided in this act."

Section 63-206, Oregon Compiled Laws Annotated:

"Neither husband nor wife is liable for the debts or liabilities of the other incurred before marriage, and except as herein otherwise declared they are not liable for the separate debts of each other, nor is the rent or income of such property liable for the separate debts of the other."

Thus, as a matter of law, Bernice was a party to both the executory contract to sell and the consummated sale. She was, by every intendment of law governing the results of the transaction, a joint purchaser of the property transferred. In truth, the lower Court did not hold that the legal results of the transaction were otherwise. It simply ignored the legal results of the transaction disclosed by the evidence. If, as the lower Court concluded, Bernice was a mere "nominal party to the transaction", then it must be because she was a wife. No other evidence appears from the record to support such a conclusion. If, as the lower Court further concluded, "it was not the intention of any of the parties that she acquire the real ownership of either the partnership interest or the corporation stock", then, again, it must be because she was a wife. No other evidence appears from the record to support such a conclusion.

To achieve internal consistency in its theory of unreality, the lower Court was forced to make the incongruous finding that O. Phil Nordling did not intend to sell or sell any part of his partnership assets or stock to his sister-in-law, Bernice Nordling. It is said that "Phil was unaware of any arrangement between Gill and Bernice until the contract was presented to him for execution, but having no interest in their dealings he made no objection" (R. 211). In making this finding as to the participation of O. Phil Nordling in the transaction, the Court

ignored the testimony of O. Phil Nordling that he intended to sell and did sell to his sister-in-law an undivided one-half interest in the partnership assets and stock transferred in the sale (R. 132-134, 138-139.)

The lower Court found that Bernice Nordling participated in the purchase of property from O. Phil Nordling and formation of the partnership "on tax considerations only", and that "The suggestion that Bernice should be taken in as a partner appears to have originated from a conference with a tax consultant" (R. 212). There is not a scintilla of evidence to support the inference of a tax-saving motive. Thus, the true motive for the participation of Bernice Nordling in the transactions is stated in the testimony of Gill Nordling as follows (R. 53):

> "Well, we had the—we had the opportunity of going into business for ourselves, either that or selling out to Phil, and the price was such that we couldn't sell out, we had to buy. Then we had to arrive at a conclusion how we were going to operate, and we decided that we wanted a partnership; I wanted her in there with me for definite reasons, and those was that she had judgment and decision which I needed because I had never operated as an individual before, I had always been in partnerships or corporations, and I needed help and I needed it badly, and I couldn't find anybody else at that time that I would want to go into business with, so the natural course was to go into business with my wife on a partnership."

On the other hand, the inference of tax-saving motive was drawn from the following testimony of Spencer R. Collins, accountant (R. 144-145):

"Q. Did you tell him there would be a substantial tax savings or that there would be some tax savings by taking his wife in as a partner?

"A. I don't recall to what extent we discussed that. As a matter of fact, the earnings were not so great as to make that a material factor.

"Q. Would you say definitely that you didn't tell him there would be tax savings?

"A. He might have asked me if there would be, we might have talked about it, but he would know as much about it as I would.

"Q. I am asking you.

"A. We probably discussed it a little, yes.

"Q. You did talk to him about tax savings?

"A. I didn't encourage him to take a tax savings and form an organization on that account."

Thus, contrary to the testimony of Spencer R. Collins that the wife did not participate in the transactions to save taxes, and contrary to the testimony of Gill Nordling that the wife participated for sound business reasons, the Court made the finding that the wife participated in the purchase and partnership formation "on tax considerations only". It is from such surmise that the straw man of unreality is said to exist.

The lower Court further found "that Bernice had no separate property; that while she had joined in the execution of the notes to carry into effect the purchase and sale contract between her husband and his brother, her credit was in no way relied on" (R. 212). In so finding, the Court ignored the fact that neither Gill Nordling nor Bernice Nordling put up any credit to secure either the unpaid portion of the purchase price, or the bank loan obtained to make the down payment, other than the property acquired by said parties as the result of the purchase (R. 62-63, Pet. Ex. No. 6; R. 82-83, 116-118). The only security given to O. Phil Nordling for the $15,500.00 note evidencing the unpaid part of the purchase price consisted of two assignments, one executed by Gill Nordling and the other by Bernice Nordling, assigning for security purposes the stock acquired by the assignors in the purchase (R. 62-63; Pet. Ex. No. 6). The only security held by the bank for the $6,000.00 note evidencing the bank loan obtained to make the down payment was a promissory note owned by Nordling Finance Co., the corporation whose stock was acquired by Gill Nordling and Bernice Nordling in equal shares (R. 82-83, 116-118). Further, the Court ignored the fact that the matter of the purchasers' credit was beside the point since the property sold had a value in excess of the purchase price (R. 102, 123, 136, 143, 128-129; Pet. Exs. Nos. 32, 34). Thus, according to the holding of the Court below, a wife is not privileged to acquire prop-

erty for tax purposes without available credit, even though she in fact bought such property at a highly favorable price and solely on the security of the property interests acquired in the purchase. The unreality in this case exists, not in the definitive transactions consummated by the parties, but in the conclusions reached by the Court as to the significance of said transactions for "federal income tax purposes".

The lower Court cites as authority for its conclusions in this case *Lusthaus vs. Commissioner of Internal Revenue,* 327 U. S. 293, 66 S. Ct. 539, and *Commissioner of Internal Revenue vs. Tower,* 327 U. S. 280, 66 S. Ct. 532. In the Lusthaus case, the husband executed a bill of sale to his wife by which he purported to sell her an undivided one-half interest in a business owned and operated by the husband. The wife paid the purchase price for the one-half interest in part with funds given to her for that purpose by her husband, and as to the remainder with funds withdrawn out of income of the business. Contemporaneously with the transfer as aforesaid, the husband and wife formed a partnership under which the business continued as it had been before. No new capital acquired by the wife from a third party was contributed by her to the partnership. The Court held that since the husband's economic interest in the business had not changed, the wife's interest in the partnership could not be recognized for federal income tax purposes.

In the Tower case, the husband transferred to his wife 190 shares, out of a total of 500 shares outstanding, of stock in a corporation. The transfer was by gift. Three days after the stock transfer, the corporation was dissolved and a limited partnership formed to continue the business. The wife contributed to the partnership her share of the assets of the dissolved corporation, and received in consideration thereof a limited interest in the partnership. The conduct of the business was not in any way altered by the corporate dissolution or the formation of the partnership. The Court held that the wife's partnership interest could not be recognized for federal income tax purposes because the formation of said partnership did not bring about a real change in the economic relation of the husband and wife to the income of the business.

In both the Lusthaus and Tower cases, the husband undertook to vest in his wife a fractional interest in a business which he had theretofore owned and operated. No additional capital or services were contributed by the wife to the partnership which was not available to the husband prior to such transfer of interest to the wife. No business purpose was served by the transfer of an interest to the wife or by the creation of the wife's partnership interest. However, in the Tower decision, the Court points the way to a bona fide partnership between husband and wife. Thus, it is said (327 U. S. 280, 290):

> "There can be no question that a wife and a husband may, under certain circumstances, become partners for tax, as for other, purposes. If she either invests capital originating with her *or* substantially contributes to the control and management of the business, *or* otherwise performs vital additional services, *or* does all of these things she may be a partner as contemplated by 26 U. S. C., §§ 181, 182. The Tax Court has recognized that under such circumstances the income belongs to the wife." (Italics supplied.)

Thus, if a wife contributes to the partnership "capital originating with her" then her interest in the partnership is recognizable for federal income tax purposes. It is evident that this conclusion is predicated on the basic principle heretofore referred to that income from property is taxable to the person who owns the property.

Thus, the decisions in *Lusthaus vs. Commissioner of Internal Revenue, supra,* and *Commissioner of Internal Revenue vs. Tower, supra,* far from being authority for the holding of the lower Court, are authority for the recognition of the interest of Bernice Nordling in the partnership assets and stock purchased by her from a third party. In this case, Bernice Nordling contributed to Nordling Parts Co. capital originating with her. The partnership assets and stock which she purchased from O. Phil Nordling must have originated with her because such property did not and could not originate from any

other source. Bernice Nordling did not acquire said property from her husband, Gill Nordling, by gift or purchase as in the Lusthaus and Tower decisions, because the ownership of said property at no time vested in Gill Nordling. It is impossible for an individual to transfer by gift or purchase property which he does not own. To hold that the partnership assets and stock acquired by Bernice Nordling originated with Gill Nordling, solely because Gill negotiated the contract of purchase in his own behalf and in behalf of Bernice Nordling as her agent, is to predicate substantial income tax liability on hypothesized facts. It is a disregard of the basic principles of local law governing ownership of property. Here, the lower Court has cited the Lusthaus and Tower cases as authority for its holding, and then has proceeded to a decision which is in direct opposition to the concepts formulated in the Lusthaus and Tower cases as to the proper tax treatment of income derived from property originating with the wife.

The decision of the lower Court in this case is not only contrary to the decisions of this Court but is in rank conflict with the decision of the United States Circuit Court of Appeals for the Eighth Circuit in *Durwood vs. Commissioner of Internal Revenue,* 159 F. (2d) 400. In the Durwood case, the husband, his three brothers and son were members of a partnership prior to January 3, 1940. On January 3, 1940, the wife was admitted to the partnership with a 25%

interest therein. In order to create the 25% interest in the wife, the interests of two of the brothers were reduced from 20% to 10% each and the interest of the son was reduced from 20% to 15%. The interest of the husband was not reduced as a result of the creation of a partnership interest in the wife. In other words, as in this case, the wife acquired her interest in the partnership from persons other than the husband. As the Court pointed out, the creation of the partnership interest in the wife did not and could not reduce the husband's income or tax liability because he did not part ownership with anything he ever owned. The partnership profits which accrued to the wife in her partnership account were left untouched by her to her credit on the books of the partnership. The only capital contributed by the wife to the partnership consisted of certain leases on motion picture theatres which she was able to obtain as lessee through her husband. The partnership engaged in the operation of motion picture theatres and the only service which the wife rendered to the partnership was the occasional previewing of motion pictures. The Circuit Court of Appeals for the Eighth Circuit reversed The Tax Court and held that the interest of the wife in the partnership was recognizable for federal income tax purposes. In so holding, the Court cited *Alexander vs. Commissioner of Internal Revenue*, 6 T. C. 804, with approval and commented on the decision in that case as follows:

"The only basis upon which it could be held that the income was taxable to the petitioner is that he had diverted a part of his income to others, members of his family, but that is not this case. A somewhat similar situation was presented to the Tax Court in S. Kenneth Alexander vs. Commissioner of Internal Revenue, 6 T. C. 804. In that case the taxpayer owned a three-fourths interest in a businss and an uncle owned a one-fourth interest. The taxpayer made arrangements for his wife to buy the uncle's interest. The purchase price of that interest was $35,000, of which $30,000 was provided by a bank loan made on the note endorsed by taxpayer and further secured by collateral of the taxpayer. The court held that the resulting partnership between the taxpayer and his wife should be recognized for federal income tax purposes. The distinction which the Tax Court found between the Alexander case and the Tower and Lusthaus cases was that the wife had received her interest from an uncle rather than from her husband, even though the husband had made it possible for her to secure the money with which to purchase the interest. The Tax Court said: 'This one-fourth did not originate with or come to the wife from the petitioner. * * * It was purchased from the uncle. * * * The loan of his name as endorser, which cost him nothing, likewise fails to indicate sham or unreality in the uncle's sale to petitioner's wife. We see nothing here that a husband might not reasonably do in assisting his wife, and not him-

self, to acquire another's partnership interest.' See, also, Harry Shulak vs. Commissioner, T. C. Decision No. 6654, April 30, 1946, 6 T. C. 1260."

Thus, in entering a reversal in the Durwood case, the Circuit Court of Appeals for the Eighth Circuit did nothing more than correct an error in law committed by The Tax Court in failing to apply a basic principle previously recognized and applied by The Tax Court in the Alexander case. In so doing, the appellate court made the following statement with respect to the jurisdiction of the Circuit Courts of Appeal in reviewing decisions of The Tax Court:

> "The Commissioner contends that petitioner could command the income of the partnership at will, and hence, whatever was taken from his brothers and given to his wife, son and daughter as income in reality came from him. The extent to which fact findings of the Tax Court are conclusive on review has often been stated, but there must be some evidence to sustain them. If there is no evidence in support of the finding, the decision can not, of course, stand. An inference or hypothesis that absent the added partners the brothers would have permitted the same income shifts to petitioner is purely speculative and not a fact. The order of the Tax Court is therefore reversed and the cause remanded with directions to enter order in conformity with this opinion."

The Durwood case announces principles which cannot be lightly cast aside. The protection of the

public revenue requires that a husband may not allocate his income to other members of his family by dividing up a business which he owns and operates. Protection of the public revenue does not require that a wife be denied the same privilege as that enjoyed by other citizens, i.e., the privilege of purchasing, owning, and deriving the income from, real and personal property. It is not a matter of public concern that a wife owns and derives income from property which her husband had an opportunity to purchase. It is not a matter of public concern that the tax liability on income derived by husband and wife from certain property is lower than the tax liability which would result if all of said property were owned by either husband or wife. If such were not the case, then spouses would be required by law to own property so as to always produce the maximum in tax liability.

Likewise, the decision in this case is contrary to basic principles previously recognized and applied by The Tax Court of the United States in other cases. Thus, in *Alexander vs. Commissioner of Internal Revenue,* 6 T. C. 804, the wife purchased a one-fourth interest in an existing partnership from her husband's uncle. After the transfer, the partnership continued with the wife owning a one-fourth interest therein. The husband was a member of the partnership before and after the purchase by the wife. The husband was a party to the agreement wherein

the uncle agreed to sell the partnership interest to the wife for $35,000.00. The bill of sale was executed to the wife. The wife made a payment of $5,000.00 on the purchase price with funds which had been withdrawn from the business prior to the purchase pursuant to a Trust in favor of the wife which the Court refused to recognize for tax purposes. The balance of the purchase price was paid with the proceeds of a bank loan. The husband endorsed his wife's bank note for $30,000.00 and put up all of the security for the note. The wife paid off the bank loan with funds obtained as follows:

Loan from husband to wife.....	$12,000.00
Loan from husband's parents to wife..	9,000.00
Profits withdrawn from partnership..	7,000.00
Paid directly by husband to bank.....	2,000.00
	$30,000.00

The loans obtained by the wife from her husband and husband's parents were repaid out of profits withdrawn from the business. No articles of partnership were ever executed by the husband and wife. The wife was not authorized to sign checks on the partnership bank account. The Court recognized the one-fourth interest of the wife in the partnership for federal income tax purposes, and in so doing made the following instructive statement:

> "Upon the facts of this case, we must now answer, as to the purchased quarter interest,

the question posed in these husband and wife partnership cases: 'Did the husband, despite the claimed partnership, actually create the right to receive and enjoy the benefit of the income, so as to make it taxable to him?' (*Commissioner vs. Tower, supra.*) This one-fourth did not originate with or come to the wife from the petitioner, as is the situation in the cases cited by the respondent, and many others involving this general question. It was purchased from the uncle, and the gist of the question is, in a large sense, who purchased it, petitioner or his wife? In our view, she did so. He signed the agreement with the uncle, but on the face of the instrument it is apparent that he did so merely to agree to the sale of the partnership interest, a prerequisite to any properly conducted sale of such interest, and to agree, together with his wife, that all partnership debts should be paid, relieving the uncle from that liability. Nothing in the instrument indicates that petitioner was purchaser. He was not a grantee in or signatory to the bill of sale from the uncle and wife to Helen Alexander, whereby the one-fourth partnership was conveyed.

"On the question of contribution of capital to the partnership, we have here in large part no mere transfer from husband to wife, as in *Commissioner vs. Tower, supra,* and *Lusthaus vs. Commissioner,* 327 U. S. 293, and many other cases. The $30,000 note was repaid. To the extent of $9,000 it was repaid by loans from petitioner's father and mother, and there is no showing that petitioner had any connection with such

loans. The quarter interest purchased from the uncle itself produced $12.101.79 in 1940 (and the wife received title on January 2, 1940), and $11,311.55 in 1941, which is more than sufficient to repay the $21,000 borrowed from petitioner and his parents, and which was repaid to them. Thus, it appears that the petitioner contributed only $2,000, for which he was not reimbursed, and the fact that $12,000 was a loan, repaid to him, is some indication that the other $2,000 was also a loan. The mere fact that it had not been repaid at time of trial does not prove otherwise. Considering the earnings of the quarter interest, it is apparent that only $5,000 of the $35,000 purchase price is shown to have originated with the other quarter interest held in trust, the income of which we have held belonged to petitioner, and thus to have originated with him, making $7,000 not orignating with the wife. (The earnings and withdrawals from the trust quarter interest are, in the absence of explanation, sufficient to cover her other expenditures.) We think that such fact is not sufficient, under all the circumstances here, to place this case in the same category with those where the entire capital contribution arose from the earnings in the partnership of the party held taxable. The uncle from whom this quarter interest came is not the petitioner here. We held, in effect, in *Carlton B. Overton*, 6 T. C. 304, and in *Abe Schreiber*, 6 T. C. 707, that, though income was taxable to a husband, a gift thereof to the wife was effected by her receipt of the income with the husband's consent, and property purchased

by her therewith was her own. Under all the facts, we think that principle is applicable here, where the amount is only one-fifth of the purchase price, from one not the husband or petitioner, where it is not shown that tax avoidance was the motive, but where one partner wished to sell and it was desired to keep the business in the family, in accordance with many years custom. Mere desire to reallocate family income is not demonstrated by the respondent, with the burden of proof. We may not here regard a gift of $2,000 by husband to wife (if in fact it is not loan, like the other $2,000, and still to be repaid) as determinative proof that the husband was the real purchaser. The loan of his name as endorser, which cost him nothing, likewise fails to indicate sham or unreality in the uncle's sale to petitioner's wife. We see nothing here that a husband might not reasonably do in assisting his wife, and not himself, to acquire another's partnership interest."

In referring to the Alexander case, The Tax Court, in its opinion in this case, states that some of the basic facts in the Alexander case are similar to the facts in this case. The Court failed to point out wherein the basic facts in the two cases differ. It is submitted that the two cases differ only as to facts which are not basic. In both cases, there existed partnerships which had been operated by members of the same family for many years. In both cases there existed a strong motivation to keep control of the business in the family. In both cases the husband

joined with the wife in the contract of purchase. In both cases the wife paid the purchase price with funds which, in the last analysis, constituted profits of the business in which the wife acquired an interest. If there is any basic difference in facts in the two cases, it is because the wife performed no services for the partnership in the Alexander case, whereas in this case Bernice Nordling rendered services for the partnership.

The only clue to the Court's reasoning in refusing to follow the Alexander decision in this case is the statement of the Court that it was "persuaded of the reality of the transaction" in the Alexander case. It appears that the Court was not so persuaded here. In both cases, there is nothing more involved, upon which persuasion as to the intention of the parties can properly be based, except the established legal results attained by the consummation of definitive transactions. The intention of the parties must be derived from the consummated legal transactions in which they voluntarily participated. It is an unreasonable inference that any of said parties intended to accomplish any result other than the legal results attained by the documents executed and delivered. The result attained, as was clearly intended by the parties, was a purchase by Bernice Nordling of one-half of the partnership interest and stock transferred by O. Phil Nordling. The Tax Court undertakes to further distinguish the Alexander case on the grounds that there the respondent had the burden

of proof, since the deficiency in tax involved in the issue was first asserted in respondent's answer, whereas here the petitioners have the burden of proof. Since the facts in the Alexander case were sufficient to cause failure of proof as to the lack of bona fides with respect to the intention of the parties therein involved, how is it that an analogous set of facts in this case is insufficient to establish the bona fides with respect to the intention of the parties here involved? In both cases, the intent of the parties must be gathered from the acts done. Acts of equivalent legal signficance must be of equal efficacy in the drawing of inferences as to intent. The acts done in this case and in the Alexander case were of virtually identical legal significance. In both cases the wives purchased property from third parties in definitive transactions.

In *Shulak vs. Commissioner of Internal Revenue*, Tax Court Memorandum Decision, Docket No. 6654, April 30, 1946, 1946 Prentice-Hall Tax Court Memorandum Decisions, para. 46,101, the wife purchased property from a third party and thereafter contributed said property to a husband and wife partnership. Also, the wife acquired other property from the husband by gift and contributed said property to the partnership. The Court upheld the wife's interest in the partnership on the grounds that the case did not involve the usual circumstances of a transfer of a fractional interest in an existing business from the husband to the wife. The Court also

pointed out that the gift of property was unrelated to the formation of the partnership. The Tax Court reapplied the concepts formulated in the Alexander and Shulak cases in the recent decision of *Forsythe vs. Commissioner of Internal Revenue,* 10 T. C. No. 54.

With respect to the decision of the lower Court concerning the acquisition by Bernice Nordling of stock of Nordling Finance Co., said decision is in conflict with a group of cases other than those hereinbefore cited dealing with a wife's interest in a business partnership. The dividends derived from the stock constituted income arising from the mere ownership of property and not profits from a husband and wife partnership. The Tax Court of the United States, and the United States Circuit Courts of Appeal, have uniformly held that income derived from mere ownership of property by a wife is taxable to the wife. In such cases, the Courts have not looked behind the crucial fact of ownership nor shifted the incidence of taxation to the husband on a theory of unreality. Nevertheless, here the Court has refused to apply the established principle of ownership. With reference to the stock ownership, the Court has reached a conclusion outside the record, outside the established legal principles applied in determining the tax liability of other taxpayers, and outside the bounds of reason, all for the mere purpose of fortifying its conclusion as to the taxability of the income from the husband and wife

partnership. The record is plain that the ownership of the stock vested in Bernice Nordling within every requirement known to the law (R. 59-60, Pet. Ex. No. 5; R. 62-63, Pet. Ex. No. 6).

Thus, on the matter of stock ownership, the decision of the lower Court in this case is in conflict with the decision of the United States Circuit Court of Appeals for the Fifth Circuit in *Allen vs. Beazley*, 157 F. (2d) 970. There, a husband, wife and son entered into a contract for the joint purchase and ownership of securities. The husband negotiated the purchase of the securities in behalf of his wife and son as undisclosed principals. The participation of the wife and son in the purchase was not divulged at the time of the sale to either the sellers or the bank from which a purchase money loan was obtained. The bank loan was paid off out of the income from the securities purchased. The agreement between the husband, wife and son provided that each owned a one-third interest in the securities. The Court upheld the interests of the wife and son and decided that each of said parties was taxable as to one-third of the income derived from the securities. Pertinent to the matter of the negotiations conducted by Gill Nordling for Bernice Nordling in this case are the following comments of the Court in the Allen decision (157 F. (2d) 970, 973):

> "We are aware of no law, state or federal, that prevents persons, whether members of the same family or not, from constituting one of their

number as an express trustee to act in his name for and on their behalf in the acquisition of property, but on the contrary we are well aware of the universal rule that where one while acting in behalf of another acquires property in his own name, a constructive or resulting trust in such property so acquired is generally created. We also recall that secret trusts or contracts embracing undisclosed principals are generally ineffectual against bona fide creditors and purchasers for value. But no rights of creditors or third parties here are in any wise jeopardized by the failure of the taxpayer to make known the interest of members of his family in the purchase of securities. The bank and the seller were paid in full. They are not here complaining of the failure to reveal the undisclosed principals for whom the taxpayer was acting. The Commissioner of Internal Revenue cannot complain for the reason that the joint purchase of the securities was made known to him from the beginning. We are mindful, too, that family partnerships in an operating business in which some members of the family contribute neither money nor services in the management or operation of the business are often regarded as unreal or spurious in determining the income tax consequences. This, however, is not a family partnership, nor is there any question of operation of the business involved. The sole question is whether there was an actual, bona fide purchase and ownership of the securities by the three members of the family. This has been proven and found by the Court below whose

finding is not only supported by the evidence but is without substantial contradiction."

It is apparent that there is no rational basis upon which the facts in this case can be distinguished from those in *Allen vs. Beazley, supra.* The difference in the two decisions lies solely in the fact that the United States Circuit Court of Appeals for the Fifth Circuit adhered to the basic principle of property ownership in *Allen vs. Beazley, supra,* whereas here the United States Circuit Court of Appeals for the Ninth Circuit refused to abide by said basic principle. Since the entire structure of the income tax laws is based on the principle that income from property is taxable to the owner of the property, the decision in this case is fundamentally wrong and should be reversed. See also *Commissioner of Internal Revenue vs. Hart,* 76 F. (2d) 864, for a case in which the United States Circuit Court of Appeals for the Sixth Circuit adhered strictly to the basic principle of taxing to a wife the income from property owned by the wife.

As to the matter of stock ownership by Bernice Nordling, the decision in this case is not only in conflict with the decisions of other United States Circuit Courts of Appeal but is in conflict with the basic principles previously recognized and applied by The Tax Court of the United States in other cases. Thus, in *Greene vs. Commissioner of Internal Revenue,* 7 T. C. 142, it was held that one-half of the rent-

als from real property owned by husband and wife as tenants by the entireties was taxable to the wife. The Respondent has promulgated an administrative ruling in keeping with the decision in the Greene case in I. T. 3743, 1945 C. B., page 142. In *Rosborough vs. Commissioner of Internal Revenue,* 8 T. C. 136, The Tax Court upheld the bona fides of the sale of corporate stock by a husband to his wife and further held that the dividends declared on said stock after the sale were taxable to the wife and not to the husband. In *Sandberg vs. Commissioner of Internal Revenue,* 8 T. C. 423, it was held that the income realized from the sale of houses and lots, where the land was owned by the husband and wife as tenants by the entireties and the husband erected houses thereon, was taxable one-half to the wife and one-half to the husband. In *Boozer vs. Commissioner of Internal Revenue,* Tax Court Memorandum Decision, Docket No. 9297, August 28, 1947, 1947 Prentice-Hall Tax Court Memorandum Decisions, para. 47,248, the husband transferred stock in a corporation to his wife and sister by gift in 1937. On January 1, 1941, a partnership was formed in which the wife and sister acquired fractional interests in consideration of their transfer to the husband of said corporate stock acquired by gift. The Court upheld the interests of the wife and sister in the partnership for income tax purposes because the wife and sister had contributed to the partnership capital originating with them. The significance of

this decision is contained in the following quotation from the decision:

"We are not here, therefore, confronted with a situation where the arrangement for family participation in a partnership was made for the express purpose of reducing taxes and as an incident to that arrangement a purported gift of an interest in the partnership was made by the husband to the wife. Cf. Commissioner vs. Tower, 327 U. S. 280 (34 AFTR 799). After it was decided to continue the business as a partnership petitioner could not transfer corporate stock to his wife and sister pursuant to his agreement. He, therefore, transferred to them in lieu of such stock, and with their consent, portions of his partnership interest equal in value to the stock which he had obligated himself to transfer to them, and at least equal in value to Woodstock shares which he had received from them. In effect, petitioner caused the partnership interests to be transferred to his wife and sister, respectively, for good and valid consideration and for full value even though the consideration had been received by him before the transfers. It is apparent, therefore, that there is no element of gift involved in the transfers of interests in King & Boozer to petitioner's wife and sister. We also think it clear that each of the women invested her own capital, which was capital originating with her within the meaning of Commissioner vs. Tower, supra.

"As pointed out by the Supreme Court in the Tower case 'if she (the wife) *either invests cap-*

ital originating with her or substantially contributes to the control and management of the business, or otherwise performs vital additional services, *or does all of these things*, she may be a partner' within the meaning of the Internal Revenue Code. (Italics supplied.) The Supreme Court made it clear that if the wife's participation either met any one or all of the tests enunciated by it, that she might be a partner. Taking all of the circumstances of the partnership here before us into consideration, as suggested by the Supreme Court in Commissioner vs. Tower, we conclude that the partnership was real within the meaning of the Federal revenue laws and that the respondent erred in taxing to petitioner one-half of the entire net distributable income of the partnership which existed in 1941."

See also *Woosley vs. Commissioner of Internal Revenue*,[1] Tax Court Memorandum Decision, Docket No. 2981, December 6, 1946, 1946 Prentice-Hall Tax Court Memorandum Decisions, para. 46,283. On the matter of stock ownership, as with the matter of assets contributed by Bernice Nordling to the partnership, the decision in this case is contrary as a matter of law to decisions from other United States Circuit Courts of Appeal and to basic principles recognized and applied in other cases decided

1. *Woosley vs. Commissioner of Internal Revenue*, Tax Court Memorandum Decision, Docket No. 2981, December 6, 1946, 1946 Prentice-Hall Tax Court Memorandum Decisions, para. 46,283, was reversed and remanded in *Woosley vs. Commissioner of Internal Revenue*, United States Circuit Court of Appeals, Sixth Circuit, No. 10586, June 2, 1948.

by The Tax Court of the United States. It is fair to conclude that this case would never have arisen if Bernice Nordling as sole purchaser had purchased the entire interest of O. Phil Nordling in the partnership assets and stock, or had purchased a part of such property interests in a transaction separate from the purchase by her husband of the remainder of said property. To deny the ownership by Bernice Nordling of the property purchased, solely because she joined with her husband as a joint purchaser, is to draw a distinction too fine for comprehension, and to ignore the fact that a basic difference between the facts here, and the facts in the above-cited cases which reach a contrary and sounder result, does not exist.

The position of O. Phil Nordling in this case is that of an innocent by-stander who receives the impact of a misdirected blow. Again, to be consistent with the hypothesis of unreality, the lower Court disallowed the loss incurred by O. Phil Nordling on the sale of stock to his sister-in-law, Bernice Nordling. The sale is deemed one made to the taxpayer's brother and thus the loss thereon disallowable under Section 24(b) of the Internal Revenue Code (United States Code, Title 26, Section 24(b)). The record is unequivocal that O. Phil Nordling intended to sell and did sell the stock to Bernice Nordling (R. 132-133, 138-139). There is no intimation in the decision of the lower Court as to how O. Phil Nordling's tax liability can be determined on the basis of any deci-

sion as to the unacceptability for tax purposes of any arrangement between Gill Nordling and Bernice Nordling. His rights are waived aside as a make-weight in support of the conclusion that Bernice Nordling's purchase of property is not recognizable for tax purposes. This disposal of the rights of O. Phil Nordling hardly assumes the dignity of a judicial determination. The decision of the lower Court in this regard is diametrically opposed on the facts and law to the decisions of The Tax Court of the United States in *Simister, Jr. vs. Commissioner of Internal Revenue,* 4 T. C. 470, and in *Saul vs. Commissioner of Internal Revenue,* Tax Court Memorandum Decision, Docket No. 7679, June 26, 1947, 1947 Prentice-Hall Tax Court Memorandum Decisions, para. 47,178.

CONCLUSION

Division of family income is beyond controversy a matter for close scrutiny by the courts. Ostensible property interests of a wife have been disregarded for tax purposes where a husband has, for no apparent reason except to save income tax, divided his unitary business operation into several economic units by formation of a partnership with other members of his family. The Courts reiterate in such cases that realism must prevail and that income must be taxed to the person who produces such income. However, if realism is to prevail in tax matters, then let it be exercised with equal justice to all.

The lower Court, in this case, has refused to apply established concepts with respect to contribution by a wife to a family partnership of capital purchased from a third party. This has been done on the vague grounds that the Court was not persuaded as to the bona fide intent of the parties. The Court was not so persuaded despite the fact that the parties obviously intended the normal legal results attained by the definitive transactions consummated. It is truly inconceivable that, regardless of the tax consequences that flow therefrom, a husband may not permit his wife to purchase income producing property which the husband has an opportunity to buy. It is beyond understanding that a husband is taxable on income produced by property owned by his wife solely because he could have initially purchased said property which was in fact purchased by his wife. In this case, Bernice Nordling purchased one-half of the partnership interest and stock transferred by O. Phil Nordling and on the basis of established legal principles is taxable on the income from said property.

Respectfully submitted,

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In the Supreme Court of the United States

OCTOBER TERM, 1948

No. 105

O. PHIL NORDLING AND GILL NORDLING, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion of the Tax Court (R. 166-185) is not reported. The opinion of the Circuit Court of Appeals (R. 210-213) is reported at 166 F. 2d 703.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on March 23, 1948. (R. 214.) The petition for a writ of certiorari was filed on June

18, 1948. The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether a partnership having federal income tax significance existed between Gill Nordling and his wife, Bernice.

2. Whether Gill Nordling should be taxed on the dividends from corporate stock held in the name of his wife.

3. Whether O. Phil Nordling should be allowed a capital loss on the sale of corporate stock—the answer being dependent upon whether the transactior was between members of a family within the meaning of Section 24(b)(1)(A) of the Internal Revenue Code.

STATUTE INVOLVED

Internal Revenue Code:

SEC. 22. GROSS INCOME.

(a) [as amended by Sec. 1, Public Salary Tax Act of 1939, c. 59, 53 Stat. 574] *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from

professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

(26 U.S.C. 22.)

SEC. 24. ITEMS NOT DEDUCTIBLE.

* * *

(b) Losses from Sales or Exchanges of Property.—

(1) *Losses disallowed.*—In computing net income no deduction shall in any case be allowed in respect of losses from sales or exchanges of property, directly or indirectly—

(A) Between members of a family, as defined in paragraph (2)(D);

* * *

(2) *Stock ownership, family, and partnership rule.*—For the purposes of determining, in applying paragraph (1), the ownership of stock—

* * *

(D) The family of an individual shall include only his brothers and sisters (whether by the whole or half blood),

spouse, ancestors, and lineal descendants; and

* * *

(26 U.S.C. 24.)

STATEMENT

The facts, as found by the Tax Court (R. 167-179) and as recited in the opinion of the court below (R. 210-212), may be summarized here as follows:

The petitioners, O. Phil and Gill Nordling, are brothers who during 1941 were operating, as a partnership under the name "Nordling Parts Company", two automobile parts stores in Oregon. They also owned substantially all of the stock of the Nordling Finance Company, a corporation which owned and rented to the partnership the physical equipment used in the partnership business. (R. 167-168.)

In August, 1941, after a preliminary exchange of letters, Phil Nordling offered (by letter dated August 19, 1941) to sell to Gill Nordling for $18,500 his partnership and corporate interests, or to buy the interest of Gill Nordling for the same price.[1] On August 28, 1941, Gill Nordling accepted

[1] This offer was made pursuant to a "buy or sell" provision contained in their partnership agreement (Resp. Ex. F, one of the exhibits which were not included in the printed record on review, but were transmitted in their original form, pursuant to order of the court below (R. 196-197)), to the effect that either partner might make an offer to buy from or sell to the other partner, and in the event of failure of the other to elect to buy or sell within thirty days the partnership was to be

Phil Nordling's offer to sell, and sent with his letter of acceptance his check for $50 to show his "good will". (R. 168-169.)

Gill Nordling turned all of these letters over to an attorney, advising him that he (Gill Nordling) and his wife, Bernice, were going to take over the business as partners, and the attorney, pursuant to Gill Nordling's instructions, prepared a formal sales contract which included the wife's name as a purchaser. Phil Nordling was unaware of any arrangement between Gill Nordling and his wife until the final papers were presented to him for execution. The suggestion that the wife be taken in as a partner originated from a conference with a tax consultant whom Gill Nordling had consulted regarding the purchase of Phil Nordling's interests. (R. 169.)

After the $50 paid with the letter of acceptance, the balance of the sales price of $18,500 was discharged by a cash payment upon the execution of the contract in the amount of $2,950, which was borrowed from a bank, and by a note in the amount of $15,500. Both notes were signed by Gill Nordling and his wife, Bernice, and both were ultimately paid out of the profits of the Nordling Parts Company. (R. 169-171.)

On September 10, 1941, six days prior to the execution of the formal contract, a partnership

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dissolved—no provision being made for selling a partnership interest to any third party.

agreement had been entered into between Gill Nordling and his wife. (R. 172-177.)[2]

At the time of the transaction here involved Bernice Nordling owned no separate property. She and her husband had four children ranging from eight to fourteen years in age. She worked for the partnership about one week in 1941, and about two weeks in each of 1942 and 1943. (R. 177.)

Under the partnership agreement, Gill Nordling was to receive a salary of $200 per month (R. 173), for his personal services. His wife withdraw $150 a month until the end of 1943, and $300 a month thereafter. While there was no evidence as to how she spent that money, Gill Nordling testified that in the later period they withdrew $600 a month for living expenses, which was approximately the total amount of the withdrawals of both. (R. 178.)

Bernice Nordling contributed to the business no services of a vital or controlling nature and no capital originating with her. She was only a nominal party to the transaction, in which her husband and his brother were the real parties in interest, and it was not the intention of any of the

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[2] The agreement, amongst other things, provided that Gill Nordling diligently employ himself in the business, and that he be its general manager—but made no provision for the performance of any services by his wife. The agreement recited contributions of capital to the partnership of some $18,000 by Gill Nordling and some $6,000 by his wife. (R. 173.) Later, in 1943, Gill Nordling, to equalize their shares as shown on the books, transferred to his wife an interest of some $4,800 on the books, and he filed a gift tax return reporting the gift. (R. 178.)

parties that she acquire the real ownership of either the partnership interest or the corporate stock for the purchase of which her husband alone had negotiated. (R. 178-179.)

Pursuant to the agreement between Phil and Gill Nordling, the stock held by them (as well as a small amount held by a third brother) in the Nordling Finance Company was surrendered, and new certificates were issued in the name of Gill Nordling and his wife. Phil Nordling sustained a long-term capital loss of $3,759.45 on the disposition of his stock. (R. 171-172.)

Upon the basis of the facts in the case, the Tax Court concluded that no partnership existed between Gill Nordling and his wife which could be recognized for federal income tax purposes, and that the real purchaser of Phil Nordling's stock was his brother, Gill Nordling. (R. 179.) Accordingly, the Tax Court sustained the Commissioner on all three questions in the case, holding in effect that all the income from the parts business and the dividends on the stock held in the name of the wife were taxable to petitioner Gill Nordling, and that petitioner Phil Nordling was not entitled to deduct any loss on the purported sale of stock to his sister-in-law since the real purchaser thereof was his brother Gill Nordling.[3] (R. 179-185.)

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[3] Petitioner Phil Nordling had conceded before the Tax Court that he was not entitled to deduct any loss with respect to that part of his stock sold to his brother, because of the provisions of Section 24(b)(1)(A) of the Code. (R. 184.)

The court below affirmed the decision of the Tax Court. (R. 210-213.)

ARGUMENT

1. The fundamental issue, upon which all three questions in the case necessarily turned (R. 179-180, 184, 212-213), was as to the reality of the transaction in which by a "last minute substitution", as the Tax Court characterized it (R. 179), the wife participated in the purchase of the partnership and corporate interests in the business which Gill Nordling had contracted to buy from his brother Phil Nordling. Upon the facts, the Tax Court, viewing her participation as "artificial in the extreme rather than real" (R. 181), concluded that the wife did not become the owner either of the partnership interest or of the corporate stock "in such a real sense" (R. 181) as to be recognized as owner for federal tax purposes (R. 180-184).

In reaching this conclusion, the Tax Court properly observed the principles enunciated by this Court in *Commissioner* v. *Tower,* 327 U. S. 280, and *Lusthaus* v. *Commissioner,* 327 U. S. 293. The court below correctly affirmed, upon the authority of those cases. (R. 212-213.) Clearly, there is no occasion for any further review of this question.

In view of the conclusion that the participation of the wife was purely nominal, the disallowance (R. 185, 213) upon the basis of Section 24(b)(1)(A) of the Internal Revenue Code, *supra,* of a deduction to Phil Nordling for a loss on the pur-

ported sale of stock to her was likewise correct, and no review is warranted upon that phase of the case.

2. Virtually the same contentions as made during the course of petitioners' extensive argument (Br. 26-60) have been considered and rejected by this Court in the *Tower* and *Lusthaus* cases and by various circuit courts of appeals in numerous subsequent cases. Certiorari was sought in many of those cases, but this Court has declined review in each instance.

Much of petitioners' argument (Br. 26-37) is really addressed to the claimed significance of portions of the evidence, the weight to be accorded thereto, the inferences to be drawn therefrom, and the like—matters clearly within the province of the Tax Court, which made findings of fact which the court below correctly held were supported by the evidence. (R. 212.)

3. Clearly, the decision below is not inconsistent with the *Tower* and *Lusthaus* cases, as urged by the petitioners (Pet. 16), who, in support of their position, point out that in those cases the husband undertook to vest in the wife a fractional interest in a business which he had theretofore owned and operated, while here, it is argued, the wife acquired an interest in the business from a third person (Br. 37-40). But the Tax Court found that the purported transaction lacked reality, and that the wife was only a nominal participant in the purchase. (R. 183.) For this same reason, there is no conflict,

as claimed (Pet. 16), with *Durwood* v. *Commissioner,* 159 F. 2d 400 (C. C. A. 8th), where the wife and children of the taxpayer were treated as having actually acquired interests in the pre-existing partnership from persons other than the taxpayer.

4. Nor is there any conflict, as urged (Pet. 17-18), with *Allen* v. *Beazley,* 157 F. 2d 970 (C.C.A. 5th), or *Commissioner* v. *Hart,* 76 F. 2d 864 (C. C. A. 6th). In the *Beazley* case, where no family partnership and no question of operation of the business were involved (157 F. 2d 974), it was held that the three members of the family were taxable upon their respective shares of the income from securities found as a fact to have been actually and bona fide purchased and owned by them; the court, concluding that the transaction had reality, stated that it is the "actuality" (*id.* p. 973) accompanying a family arrangement which determines its effect for tax purposes. Here, the arrangement having been found to lack reality, the "papers" which had been drawn up (cf. *Commissioner* v. *Tower, supra,* p. 291) were correctly held ineffective for tax purposes. Cf. *Commissioner* v. *Court Holding Co.,* 324 U. S. 331. The *Hart* case clearly has no bearing on the instant case: It holds, in view of Michigan law, taxable one-half each to the husband and wife the income received by them as vendors under a contract for the sale of Michigan land owned by them as tenants by the entirety.

CONCLUSION

The decision below is correct. It turns upon the particular facts of the case and presents no question calling for further review by this Court. There is no conflict of decisions. The petition should therefore be denied.

Respectfully submitted,

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